Taxation of Accounts Receivable in Ohio-The Impact of Constitutional Limitations

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"Taxation is an attribute and function of sovereignty."[1] This succinct statement by the Ohio Supreme Court places the taxing power in its proper perspective as one of the expressions of governmental power. The taxing power, like other governmental powers, is subject to and must be confined within state and federal constitutional limitations. As was aptly said by the United States Supreme Court in *Haavik v. Alaska Packers' Association:*[2]

> Unless restrained by constitutional provision, the sovereign has power to tax all persons and property actually within its jurisdiction and enjoying the benefit and protection of its laws.

That the power of taxation must be channeled within constitutional bounds has been shown in the experience of Ohio in the taxation of accounts receivable.[3]

In considering the taxation of intangible property certain principles are of inextricable concern:

(1) The Ohio intangible tax[4] is an ad valorem property tax.[5]

(2) State tax laws may not be given extraterritorial effect.[6]

In this respect the United States Supreme Court has said:

> While a state may so shape its tax laws as to reach every object which is under its jurisdiction, it cannot give them any extraterritorial operation.[7]

The same principle has recently been expressed by the Supreme Court in the following words:

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[1] Haefner v. Youngstown, 147 Ohio St. 58, 68 N.E. 2d 74 (1946).

[2] 263 U.S. 510 (1924).

[3] Wheeling Steel Corp. v. Glander; National Distillers Products Corp. v. Glander, 337 U.S. 562 (1949).

[4] OHIO GEN. CODE §§ 5323, 5325-1, 5327, 5328-1, 5328-2, 5388, 5389, 5638, 5638-1 and related sections.

[5] Bennett v. Evatt, 145 Ohio St. 587, 62 N.E. 2d 345 (1945).

[6] Frick v. Pennsylvania, 268 U.S. 473 (1925).

[7] *Ibid.*

> All subjects over which the sovereign power of a state extends are objects of taxation; but those over which it does not extend are exempt from taxation.[8]

(3) The property which is subjected to an ad valorem property tax must be within the territorial jurisdiction of the taxing state. This constitutional requirement is applicable to intangible as well as other property.[9]

(4) "The test of whether a tax law violates the due process clause is whether it bears some fiscal relation to the protection, opportunities, and benefits given by the state, or in other words, whether the state has given anything for which it can ask a return."[10]

(5) Being incorporeal in nature, intangible property does not have a physical situs, and therefore is presumed to have a taxable situs at the owner's domicile.[11] The attribution of a tax situs for intangibles to the state of the owner's domicile has been somewhat artifically expressed in the maxim "mobilia sequuntur personam."[12] The rule of "mobilia" which recognizes that the situs of intangible property follows the domicile of the owner is a formal and unexplanatory statement of a legal conclusion. The United States Supreme Court has placed the taxation of intangible property at the owner's domicile on a constitutional basis rather than on the legal fiction expressed under the maxim of "mobilia."[13]

The requisite connection between the taxing sovereign and the intangibles of a resident has been expressed by the court as follows:

> An adequate constitutional basis for imposing on a citizen of a state a tax on the use and enjoyment of rights in intangibles measured by their value is found in the state's control over the citizen at place of his domicile, and his duty there, common to all citizens, to contribute to the support of the government of the state.[14]

The ineluctable growth in the complexity of business activities brought about judicial recognition that intangible property could acquire a taxable situs in a non-domiciliary state.[15] The courts have held that the intangibles may acquire a business situs at a place

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[8] Curry v. McCanless, 307 U.S. 357 (1939).

[9] Wheeling Steel Corp. v. Fox, 298 U.S. 193 (1936).

[10] Wisconsin v. J. C. Penny Co., 311 U.S. 435 (1940).

[11] Blodgett v. Silberman, 277 U.S. 1 (1928); *see* Virginia v. Imperial Coal Sales Co., 293 U.S. 15 (1934); First Bank Stock Corp. v. Minnesota, 301 U.S. 234 (1937); Newark Fire Insurance Co. v. State Board of Tax Appeals, 307 U.S. 313 (1939).

[12] Blodgett v. Silberman, 277 U.S. 1 (1928).

[13] Curry v. McCanless, 307 U.S. 357 (1939).

[14] *Ibid.*

[15] Wheeling Steel Corp. v. Fox, 298 U.S. 193 (1936).

other than at the owner's domicile when such intangibles become integral parts of some local business.[16] Thus has been evolved the doctrine of a "business situs" in the taxation of intangible property. In the leading case of *Wheeling Steel Corporation v. Fox*,[17] the United States Supreme Court expressed approval of the business situs doctrine for taxing intangibles by saying that:

> The rule that the situs of intangible property for the purpose of taxation is at the domicile of the owner is subject to an exception in the case of choses in action created in the conduct by an owner of his business in a state other than that of his domicile.

The following explicatory statement as to a business situs for intangibles was made in *First Bank Stock Corp. v. Minnesota:*[18]

> The doctrine that intangibles may be taxed at their business situs, as distinguished from the legal domicile of their owner has usually been applied to obligations to pay money, acquired in the course of a localized business.

THE OHIO SITUS STATUTES AND THE JUDICIAL HISTORY THEREOF

The constitutional basis for taxation of all the intangible property of a resident[19] is recognized in Ohio by the primary provision of Section 5328-1, General Code, which states that:

> All moneys, credits, investments, deposits and other intangible property of persons residing in this state shall be subject to taxation . . . .

However, the General Assembly has not deemed it advisable for Ohio to occupy its full constitutional sphere of taxation with respect to Ohio residents, for by statutory formula Ohio has fixed the situs of intangible property within and without the state.[20] Section

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[16] *Ibid; see* Newark Fire Insurance Co. v. State Board of Tax Appeals, 307 U.S. 313 (1939); Notes, 143 A.L.R. 361 (1943).

[17] 298 U.S. 193 (1936).

[18] 301 U.S. 234 (1937).

[19] Curry v. McCanless, 307 U.S. 357 (1939).

[20] Pertinent parts of the OHIO GEN. CODE read as follows:

"Sec. 5328-1: . . . Property of the kinds and classes mentioned in Section 5328-2 of the General Code, used in and arising out of business transacted in this state by, for or on behalf of a non-resident person . . . shall be subject to taxation; and all such property of persons residing in this state used in and arising out of business transacted outside of this state by, for or on behalf of such persons . . . shall not be subject to taxation. . . .

"Sec. 5328-2: Property of the kinds and classes herein mentioned, when used in business, shall be considered to arise out of business transacted in a state other than that in which the owner thereof resides in the cases and under the circumstances following:

5328-1 further provides that intangible property of non-residents mentioned in Section 5328-2, General Code, which is used in and arises out of business transacted in this state shall be subject to taxation, and all such property of a resident which is used in and arises out of business transacted outside Ohio shall not be subject to taxation.

Section 5328-2, General Code, supplements the situs provisions of Section 5328-1 by providing that under certain circumstances intangibles shall be considered to arise out of business transacted in a state other than that in which the owner thereof resides. Sections 5328-1 and 5328-2, General Code, establish a business situs of accounts receivable in and out of Ohio. Section 5328-2 declares that the assignment of a business situs outside of this state for accounts receivable of an Ohio resident is inseparable from the assignment of such situs in this state for the intangibles of a non-resident in a like case and under similar circumstances. Attention should be focused on the following portion of Section 5328-2:

> The provisions of this section shall be reciprocally applied to the end that all property of the kinds and classes mentioned in this section having a business situs in this state shall be taxed herein and no property of such kinds and classes belonging to a person residing in this state and having a business situs outside of this state shall be taxed.

"In the case of accounts receivable, when resulting from the sale of property sold by an agent having an office in such other state or from a stock of goods maintained therein, or from services performed by an officer, agent or employee connected with, sent from, or reporting to any officer or at any office located in such other state. . . .

"The provisions of this section shall be reciprocally applied, to the end that all property of the kinds and classes mentioned in this section having a business situs in this state shall be taxed herein and no property of such kinds and classes belonging to a person residing in this state and having a business situs outside of this state shall be taxed. It is hereby declared that the assignment of a business situs outside of this state to property of a person residing in this state in any case and under any circumstances mentioned in this section is inseparable from the assignment of such situs in this state to property of a person residing outside of this state in a like case and under similar circumstances. . . .

"Sec. 5325-1: . . . Money, deposits, investments, accounts receivable and prepaid items, and other taxable intangibles shall be considered to be 'used' when they or the avails thereof are being applied, or are intended to be applied in the conduct of the business, whether in this state or elsewhere . . .

"Sec. 5327: The term 'credits' as so used, means the excess of the sum of all current accounts receivable and prepaid items used in business when added together estimating every such account and item at its true value in money, over and above the sum of current accounts payable of the business, other than taxes and assessments. . . . "

The statutory situs formula which Ohio has adopted was characterized by the United States Supreme Court[21] in the following language:

> This basic rule separates the situs of intangibles from the residence of their owners whereas it has traditionally been at such residence, though with some exceptions.

The taxation of accounts receivable under Sections 5328-1 and 5328-2, General Code, is a deviation from the "mobilia" doctrine under which all of the intangibles of a resident are subject to taxation in the state of domicile. Ohio has chosen to exempt certain accounts receivable of its residents and to exact reciprocity by taxing accounts receivable of non-residents when accounts receivable have acquired a business situs in Ohio.

Prior to the adoption of the present Ohio intangible property situs statutes in 1933, Ohio followed the common law rule of "mobilia," but also recognized that intangible property could acquire a tax situs in a non-domiciliary state when such intangibles had acquired a business situs therein.[22] The contrast between the present statutes and those which existed prior to 1933 is illustrated in the case of *Tax Commission v. Kelly-Springfield Tire Company*.[23]

The question in the *Kelly-Springfield* case was whether or not accounts receivable of a corporation domiciled in the state of New York had acquired a business situs in Ohio. At that time Section 5328, General Code, subjected all intangible property of Ohio residents to taxation.[24] The Court interpreted Section 5328 to mean that in order to tax property in Ohio the property had to be within the territorial jurisdiction of the state or had to be owned by persons residing in this state. The syllabus rules of the *Kelly-Springfield* case reflect the situs principles then adhered to in Ohio. Paragraphs 3 and 5 of the syllabus read as follows:

> 3. Generally, in absence of controlling circumstances to contrary, situs of intangible property for purpose of taxation is state of owner's domicile.
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> 5. Creation of 'business situs' for purpose of taxing credits in state where debt arises requires control and management of credits to be vested in local agency.

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[21] Wheeling Steel Corp. v. Glander; National Distillers Products Corp. v. Glander, 337 U.S. 562 (1949).

[22] Tax Commission of Ohio v. The Kelly-Springfield Tire Co., 38 Ohio App. 109, 175 N.E. 700 (1931).

[23] *Ibid.*

[24] OHIO GEN. CODE § 5328, provided in part: "All real or personal property in this state, belonging to individuals or corporations, and all moneys, credits, investments in bonds, stocks, or otherwise, of persons residing in this state, shall be subject to taxation, except only such property as may be expressly exempted therefrom."

The rulings announced in the *Kelly-Springfield* case relative to the business situs of intangible property form a background pattern for observing the contrast between the common law concept of situs of intangibles and the judicial interpretation of the existing statutory formula prescribed by Sections 5328-1 and 5328-2, General Code.

The original administrative policy relative to the tax situs of accounts receivable under Sections 5328-1 and 5328-2 was reflected in Rule 204 which the Tax Commissioner promulgated in 1939 pursuant to his authority to adopt rules provided by Section 1464-3, General Code. A dual test was imposed by Rule 204 for the ascribing of a situs of receivables in and out of Ohio. Before receivables could acquire a situs in a state other than that of owner's residence, such intangibles had to (1) "arise out of business" in a state other than that of the owner's residence within the purview of Section 5328-2 and (2) be "used in business" in the non-residential state. This dual test conformed to the provisions of Section 5328-1, General Code. Receivables were deemed to be "used in business" in the state other than that of the owner's residence when such intangibles were subject to the control and management of an officer or agent of the owner at an office in the non-residential state. This requirement that the receivables be subject to "control and management of an agent" in the non-residential state was in accord with the test for business situs announced in the previously mentioned *Kelly-Springfield* case.

The judicial history of the statutory formula for fixing situs in and out of Ohio with respect to accounts receivable evolved initially through a consideration of such statutes as applied to domestic corporations, and the concluding chapters of this history in which constitutional complications were involved, were written with respect to foreign corporations.

Starting in the year 1943, three cases[25] involving the question as to whether accounts receivable of domestic corporations had acquired a business situs out of Ohio under Sections 5328-1 and 5328-2 were presented to the Ohio Supreme Court. The interpretation of these situs statutes with respect to domestic corporations fixed the pattern of interpretation for foreign corporations because as before stated, Section 5328-2 declares that the assignment of a business situs outside this state to intangibles of a resident of

[25] The Proctor & Gamble Co. v. Evatt, 142 Ohio St. 369, 52 N.E. 2d 517 (1943); The Ransom & Randolph Co. v. Evatt, 142 Ohio St. 398, 52 N.E. 2d 738 (1944); Haverfield Co. v. Evatt, 143 Ohio St. 58, 54 N.E. 2d 149 (1944).

Ohio is inseparable from the assignment of such situs in this state to property of a non-resident.

In the case of *The Proctor & Gamble Co. v. Evatt*,[26] the Ohio Supreme Court was confronted with the situation in which a domestic corporation contended that its accounts receivable which arose from the business activities of district offices outside Ohio were not taxable in Ohio because of the provisions of Sections 5328-1 and 5328-2, General Code. The operative facts were that each of the taxpayer's district offices outside of Ohio was in charge of a district manager who performed all necessary administrative duties. The district offices deposited the checks and money received in payment on their accounts receivable in banks in the district office cities. Said district managers supervised the selling and delivery of merchandise and the collection of the resulting accounts receivable. The district managers had authority to accept drafts on the local bank accounts and to apply these deposits in the payment of the various expenses of such offices. The checks covering the expenses of the district officers were drawn on the local banks and then forwarded to Cincinnati, Ohio, to be signed by the company treasurer.

The Tax Commissioner contended that it is the basic rule of Section 5328-1 that all accounts receivable of an Ohio resident shall be subject to taxation in Ohio unless such property gains a tax situs out of Ohio under the situs statutes. The Commissioner further contended that in order for the accounts receivable of a domestic corporation to gain a tax situs out of Ohio, it was necessary under Section 5328-1 that such accounts receivable be used in business in some other state and arise out of business conducted in such other state. The Commissioner assessed the accounts receivable because it was determined that such accounts receivable were not used in business in the states where the district offices were located, for such receivables or the avails thereof were used by the Ohio corporation in the conduct of its manufacturing operations wherever occurring.

The Board of Tax Appeals[27] concluded that the accounts receivable were used in and arose out of business transacted outside of Ohio and hence were not subject to taxation in this state. In its journalized decision, the Board stated:

> . . . Looking at the pertinent provision of Sections 5328-1 and 5328-2, General Code, in the light of the definitive provisions of Section 5325-1, General Code, above noted, we are of the opinion that the accounts receivable here in question were used in and arose out of business

[26] 142 Ohio St. 369, 52 N.E. 2d 517 (1943).

[27] OHIO GEN. CODE §§ 1464, 1464-1, 1464-2 and 1464-5.

transacted outside of the state and are not subject to taxation in this state . . . .

After reciting the statutory rule that the Supreme Court may not reverse a decision of the Board of Tax Appeals unless it finds the same unreasonable or unlawful,[28] the Court concluded that the statutes and the stipulated facts supported the determination of the Board that the accounts receivable were attributable to the district offices outside of Ohio and were used by such offices in the conduct of their activities. The decision of the Board holding that the accounts receivable were not taxable in Ohio was upheld. The Court's interpretation of the statutory formula for fixing the situs of intangibles in and out of Ohio was not clearly evident in this case as it was to be in another decision.[29]

The pivotal case in the interpretation of the Ohio situs statutes is *The Ransom & Randolph Co. v. Evatt*,[30] for here the Supreme Court made manifest its interpretation of the requirements for establishing a business situs for accounts receivable in and out of Ohio. This decision clearly evidenced that the Court had concluded that the Ohio situs statutes were deviations from the common law principles of business situs.

The factual pattern in the *Ransom* case was as follows: The taxpayer was an Ohio corporation with its office, manufacturing plant and principal place of business located at Toledo, Ohio. The company had qualified to do business in the states of Indiana and Michigan and maintained retail stores in those two states. The retail stores in Indiana and Michigan were under the authority of branch managers who had the authority to purchase merchandise, to sell such merchanidse, to fix and determine the terms of sale, to enforce collection of the accounts receivable growing out of sales of goods and to make all necessary adjustments with respect to sales. The proceeds from the sales made by the branch stores were deposited by the branch managers in the cities where the stores were located. These deposits were then periodically withdrawn by the home office at Toledo and applied generally to the conduct of the corporate business including payment of the various expenses of the retail stores located out of Ohio. The company maintained its central accounting system at Toledo, Ohio.

In preparing its tax returns for the years 1939 and 1940, the corporation did not include accounts receivable which arose from the sale of merchandise by the branch stores located in Indiana and

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[28] OHIO GEN. CODE § 5611-2.

[29] The Ransom & Randolph Co. v. Evatt, 142 Ohio St. 398, 52 N.E. 2d 738 (1944).

[30] 142 Ohio St. 398, 52 N.E. 2d 738 (1944). This decision is referred to throughout the paper as the *Ransom* case.

Michigan. The Tax Commissioner determined that such accounts receivable arising in the branch stores had a tax situs in Ohio and assessment was made accordingly. The Board of Tax Appeals concluded that these accounts receivable were not used in business in such other states, and hence had not gained a business situs there so as to be exempt from taxation by Ohio, the domiciliary state.

The question as stated by the Court was "whether these intangibles have a business situs in or out of this state." In concluding that the accounts receivable were taxable in Ohio, the Board of Tax Appeals found that the accounts receivable arose out of business in the states of Michigan and Indiana within the purview of Section 5328-2 because the receivables accrued from the sales of property by managing agents having offices in those states and the property was sold from stocks of goods maintained in such other states. However, the Board took the view that a dual test was imposed under the situs statutes before accounts receivable of an Ohio corporation could acquire a business situs outside this state. The Board held that accounts receivable had to (1) be used in business in such other state and (2) arise out of business in such other state.[31] With respect to the first facet of the dual test—that the receivables be "used in business in such other state," the Board required that the receivables be so used in such other state as to become an integral part of such local business. In this view the Board adopted a standard similar to that of the common law doctrine of business situs which requires an integration of the intangibles in the local business.[32]

The assessment of the Tax Commissioner which was predicated upon the dual requirement of the receivable being used in business and arising out of business in such other state was affirmed by the Board in its decision. Attention was fixed by the Board upon the fact that the avails of the receivables arising out of the sales of goods in Indiana and Michigan were withdrawable only by the home office at Toledo, Ohio, and that such avails were expended in the conduct of the business of the company as a whole. Because of this factual pattern the Board held that such receivables were not used in business in Indiana and Michigan so as to become an integral part of such local business, and it was concluded that under the Ohio statutes such receivables had not acquired a business situs outside of Ohio.

The Ohio Supreme Court rejected the view of the situs statutes taken by the Board of Tax Appeals. While the Court was of the

[31] OHIO GEN. CODE §§ 5328-1 and 5328-2.

[32] Newark Fire Insurance Co. v. State Board of Tax Appeals, 307 U.S. 313 (1939).

opinion that Section 5328-1 requires that intangible property of persons residing in Ohio be used in and arise out of business transacted outside Ohio, the Court applied the definition of Section 5325-1, General Code,[33] to the term "used in business" and held that such term, as defined in the situs statutes, did not mean that the accounts receivable had to become an integral part of the local business. The reasoning process by which the Court concluded that the accounts receivable of the Ransom Company, which accrued from sales in Michigan and Indiana, had acquired a business situs in such states and hence were not taxable in Ohio, evolved as follows:

1. The Court referred initially to the provision of Section 5328-1 that intangible property of persons residing in Ohio which is used in and arises out of business transacted outside of this state for or on behalf of such Ohio resident shall not be subject to taxation in this state. This provision of the statute which under certain circumstances relinquishes Ohio constitutional power to tax the intangibles of its residents was commented upon by the Court as follows:

> Here is an unqualified exemption of intangibles having a business situs outside of the state. There is left for determination only the question of the business situs.

2. The Court further concluded that Section 5328-2 fixes the business situs of accounts receivable. It also pointed out that under this section accounts receivable are considered to arise out of business transacted in such other state when the receivable results from the sale of property sold by an agent having an office in such other state or from a stock of goods maintained there.

3. Having determined that the business situs of accounts receivable was fixed by Section 5328-2, the Court turned its attention to the remaining facet of the dual test of Section 5328-1 that intangibles be used in business in such other state. The meaning of the term "used in business" was found by the Court in Section 5325-1, which defines the terms "used in business" and "business." The Court referred to that part of the definitive provision of Section 5325-1 which states that intangible property shall:

> * * * be considered to be 'used' when they or the avails thereof are being applied, or are intended to be applied in

[33] OHIO GEN. CODE § 5325-1 reads in part:

"Moneys, deposits, investments, accounts receivable and prepaid items, and other taxable intangibles shall be considered to be 'used' when they or the avails thereof are being applied, or are intended to be applied in the conduct of the business, whether in this state or elsewhere. 'Business' includes all enterprises of whatsoever character conducted for gain, profit or income and extends to personal service occupations."

> the conduct of the business, *whether in this state or elsewhere.* (Emphasized by Court.)

With respect to the "used in business" requirement, the Court stated:

> For emphasis, we repeat that intangibles are to be considered as used when they or the avails thereof are being applied or are intended to be applied in the conduct of the business *whether in this state or elsewhere.* (Court's emphasis.)

Thus, the Court announced the rule that accounts receivable could acquire a business situs out of Ohio if such receivables arose out of business transacted in such other state within the purview of Section 5328-2, General Code, and if the accounts receivable were used in the general business of the taxpayer whether in this state or elsewhere so as to meet the definitive test of Section 5325-1, General Code.

It is interesting to note that the Board of Tax Appeals had previously interpreted the term "used in business in such other state" by reference to Section 5325-1, for in its entry in *The Proctor & Gamble* case[34] it was stated that Sections 5328-1 and 5328-2 were interpreted "in the light of the definitive provisions of Section 5325-1, General Code . . ." In the *Ransom* case, however, a more restrictive view of such term was taken by the Board.

In making the assessments against The Ransom & Randolph Company for accounts receivable which arose from the sales of branch stores in Michigan and Indiana, the Tax Commissioner relied upon the provisions of Rule 204, the pertinent part of which reads as follows:

> Accounts receivable shall be deemed to be 'used in business' in a state other than the residence of the owner thereof when such accounts are subject to the control and management of an officer or agent of the owner at an office in a state other than that in which the owner thereof resides.

In promulgating this rule the Tax Commissioner took the view that under the situs statutes not only must an account receivable arise out of business in such other state, but that such receivables must be used in business in such other state by being subject to the control and management of an officer or agent therein. The Court concluded that this rule of the Tax Commissioner exceeded the statutory provisions for the establishment of a business situs outside Ohio for Ohio residents, and hence it was held that the requirement of the rule for "used in business" was inapplicable. The

[34] *Supra*, note 26.

rationale of the Court's decision was clearly reflected in the following statement at page 408 of the opinion:

> The only statutory conditions for out-of-state situs of accounts receivable are that they shall be used in business and shall result from the sale of property sold by an agent having an office in such other state or from a stock of goods maintained therein (Section 5328-2, General Code).

In adverting to the rule of the Commissioner, the Court stated that the situs statutes did not require that accounts receivable be subject to the control and managment of an officer or an agent in such other state. Although Rule 204 was held to be in conflict with the statutes, the Court made the following observation as to its possible application to the factual pattern in the *Ransom* case: "However, we think that the accounts receivable in this case meet this test."

The Board of Tax Appeals in holding that the accounts receivable of the Ransom Company had not acquired a business situs outside of Ohio, had taken a common law view of the requirement that such receivables be used in business outside of Ohio. Under the Board's interpretation of Sections 5328-1 and 5328-2 the receivables were used in business in such other state only when they were so used as to become an integral part of the business carried on in such other state. As to this holding of the Board, the Court ruled that common law principles could not be relied upon to establish a business situs of accounts receivable out of Ohio because the Ohio statutes had changed the common law with respect to the situs of intangible property.[35]

With respect to the legislative intent in adopting the reciprocal situs provisions, the Court stated:

> It is clear that it was the intention of the General Assembly that all property having a business situs in Ohio should be taxed in Ohio and that no property having a business situs outside of Ohio should be so taxed.

The Court further stated that the Ohio situs statutes were enacted in order to avoid taxation of intangibles in more than one state. Reference was made to the case of *Fidelity & Columbia Trust Co. v. City of Louisville,*[36] which the Ohio Supreme Court concluded stood for the proposition that liability to taxation in one state does not necessarily exclude liability in another. It was also pointed out

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[35] In Par. 7 of the syllabus in the *Ransom* case the Court stated:

"When an unambiguous statute changes the common law on any subject, such statute is to be followed to the exclusion of any general rule otherwise applicable to cases coming within the purview of the statute."

[36] 245 U.S. 54 (1917).

that the intangibles which Ohio sought to tax were reported for taxation in the states of Indiana and Michigan. Apparently it was the view of the Court that the Ohio General Assembly patterned its situs statutes to avoid the taxation of the same intangibles in more than one state.

The Court's ruling that the "used in business" test of Section 5328-1 was met when the accounts receivable or the avails thereof were used in the general business of the taxpayer whether in this state or elsewhere as prescribed by Section 5325-1 was to precipitate constitutional complications when that theory was applied to foreign corporations.

The principles relating to business situs which were announced in the *Ransom* decision were then applied to both domestic and foreign corporations because of the mandatory requirement of Section 5328-2 that the assignment of a business situs outside of this state to intangibles of an Ohio resident requires the assignment of such situs in this state to the intangibles of a person residing outside of Ohio. The disparity between the jurisdiction of Ohio to tax a domestic corporation and a foreign corporation was brought into focus when the ruling of the *Ransom* case was applied to a foreign corporation. In the *Ransom* case the problem presented to the Court was not fraught with constitutional difficulties, for Ohio had the constitutional authority to tax all of the intangibles of an Ohio resident.[37] Rather the question in applying the situs statutes to a domestic corporation was to what extent has Ohio by the situs statutes relinquished its constitutional power to tax the intangible property of its residents.

However, a vastly different jurisdictional basis for taxation was presented when Ohio sought to tax the accounts receivable of a foreign corporation in conformity with the rationale of the *Ransom* case. The next step in the judicial history of the Ohio situs statutes took place when the Ohio Supreme Court decided the case of *National Distillers Products Corporation and Wheeling Steel Corporation v. Glander*.[38] Here the Court was presented with a situation involving the taxation of accounts receivable belonging to foreign corporations whose only nexus with the State of Ohio resulted from the fact that such receivables arose from the sale of property from a stock of goods maintained in Ohio. Applying the cognate provisions of Sections 5328-1 and 5328-2 as judicially interpreted, the Commissioner allocated the accounts receivable of these foreign corporations to Ohio because such receivables arose from the sale of property from a stock of goods located in Ohio

[37] Curry v. McCanless, 307 U.S. 357 (1939).
[38] 150 Ohio St. 229, 80 N.E. 2d 863 (1948).

and such accounts receivable or the avails thereof were used or were intended to be used by the foreign corporation in its general business whether in Ohio or elsewhere. Thus, under the reciprocal language of Section 5328-2, such receivables of these foreign corporations were determined to have a business situs in Ohio because the Ohio Supreme Court, in the *Ransom* case, had announced the rule that the statutory conditions for business situs in and out of Ohio of accounts receivable were met when such receivables were used in business as defined in Section 5325-1 and arose from the sale of property by an agent having an office in such other state, or from a stock of goods maintained therein within the purview of Section 5328-2, General Code.

The foreign corporations raised the question of the constitutional jurisdiction of Ohio to tax such receivables. Here, the constitutional basis for taxation which the United States Supreme Court has found in the protection afforded by a state to its residents was inapplicable.[39] Under traditional constitutional concepts, Ohio could tax the property of a foreign corporation only if such property were within the territorial jurisdiction of the taxing state.[40] This jurisdiction had been found in the case of intangible property owned by non-residents when such property had acquired a business situs in the taxing jurisdiction.[41]

The operative facts were these: The National Distillers Products Corporation was incorporated under the laws of Virginia. Its principal business office was located in New York where its directors conducted their meetings and its business activities were controlled. Said corporation had distilling and refining plants in seven states, including a plant at Carthage, Ohio. Its products were sold in many states. Funds for the payment of its business expenses were obtained through accounts drawn at New York on banks in that city. The accounts receivable in question were recorded in the New York office and were payable there. The accounts receivable which were assessed in Ohio arose from the sale of products manufactured at and shipped from the Carthage plant. All of the orders for the sale of products were solicited by agents outside of Ohio and such orders were subject to acceptance or rejection at the New York office. The money received in payment of such accounts receivable was used by the company in its business wherever needed.

The factual situation relative to the Wheeling Steel Corporation followed the same general pattern. The Wheeling Steel Corporation

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[39] Curry v. McCanless, 307 U.S. 357 (1939).

[40] Wheeling Steel Corp. v. Fox, 298 U.S. 193 (1936).

[41] *Ibid.*

was organized in Delaware where it maintained a statutory office, but its general offices from which the entire business was controlled were located at Wheeling, West Virginia. There all the meetings of the directors, shareholders and executive committees were held. The general books and accounting records were kept at Wheeling; collections of notes and accounts receivable stemmed from such office; four manufacturing plants were operated in West Virginia and four in Ohio and its officers at the Wheeling office have custody of its money, notes and bookkeeping records. Sales offices were maintained in twelve states including one in Ohio, and the orders taken by such offices are subject to acceptance or rejection at the Wheeling offices. The billing and collection of the accounts receivable were handled by the Wheeling office and the sales offices had no authority with respect to the collection of such receivables.

In a somewhat cryptic opinion the Ohio Supreme Court affirmed the decision of the Board of Tax Appeals which held that the accounts receivable of the foreign corporations which arose from shipments from stocks of goods in Ohio had a business situs in Ohio under the situs statutes. As it did in the *Ransom* case, the Court considered Sections 5325-1, 5328-1 and 5328-2, General Code. Reference was made to the *Ransom* decision and other decisions in which the situs statutes had been interpreted by the Court. The foreign corporations contended that the interpretation of the situs statutes adopted by the Board of Tax Appeals rendered Sections 5328-1 and 5328-2, General Code, unconstitutional under the due process and equal protection clauses of the state and federal constitutions. These claimed constitutional violations were found to be without merit and in support of such ruling the Court cited the Georgia case of *Parke, Davis & Co. v. City of Atlanta,*[42] wherein it was determined that accounts receivable of a foreign corporation which arose by deliveries of goods from warehouses in the state of Georgia were found to have a taxable situs in that state and therefore subject to ad valorem taxation.

The Ohio Supreme Court did not discuss the application of the situs statutes with respect to the intangibles of a foreign corporation but rather merely quoted the applicable provisions of the situs statutes and Section 5325-1 which defines the term "used in business." It seems apparent that the Court was fully cognizant of the fact that the reciprocal provisions of Section 5328-2 made its interpretation of the situs statutes in the *Ransom* case controlling when Ohio sought to tax the accounts receivable of a foreign corporation. In fact, the reciprocal language of Section 5328-2 compelled the application of the situs theory of the *Ransom* case as to domestic

[42] 200 Ga. 296, 36 S.E. 2d 773 (1946).

corporations to the receivables of foreign corporations.[43]

Wheeling Steel Corporation and the National Distillers Products Corporation perfected appeals to the United States Supreme Court.[44] The Ohio taxation of accounts receivable of foreign corporations which arose from shipments from a stock of goods in Ohio was challenged as being violative of the Federal Constitution. After reviewing the facts relative to the foreign corporations, the United States Supreme Court[45] pointed out that under Sections 5328-1 and 5328-2, Ohio General Code, the Tax Commissioner assessed certain accounts receivable of these corporations which were derived from shipments originating at Ohio manufacturing plants. Large portions of the Supreme Court's opinion are taken up in quoting from the entry of the Board of Tax Appeals wherein the Board held such receivables to be sitused in Ohio but lucidly pointed out that even though it felt compelled to so hold because of the decision in the *Ransom* case, it also believed that a serious constitutional question was presented when the rationale of that decision was applied to a foreign corporation.

The Court referred to that portion of the Board's entry which stated that prior to the *Ransom* decision the Board was of the view that before a business situs of intangible property could be ascribed to a state other than the state of the taxpayer's domicile it must appear that:

> 1. The intangible property arose out of business transacted in such other state, and
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> 2. The intangibles were used in such other state so as to become an integral part of the business carried on therein. [46]

By further quoting from the entry of the Board of Tax Appeals, the Supreme Court's opinion clearly shows the different interpretations which were made of the situs statutes by the Tax Commissioner and the Board of Tax Appeals and by the Ohio Supreme Court. This last requirement of "integration of the intangibles in the business of such other state" was eliminated by the Ohio Supreme Court in the *Ransom* decision, for the Court there held that Section 5328-2

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[43] OHIO GEN. CODE § 5328-2 reads in part:

"It is hereby declared that the assignment of a business situs outside of this state to property of a person residing in this state in any case and under any circumstances mentioned in this section is inseparable from the assignment of such situs in this state to property of a person residing outside of this state in a like case and under similar circumstances."

[44] 337 U. S. 562 (1949).

[45] The United States Supreme Court will be referred to herein as the Supreme Court.

[46] OHIO GEN. CODE §§ 5328-1 and 5328-2.

fixed the business situs of accounts receivable and that "used in business" meant use of the intangibles in the general business.

The Supreme Court adverted to the fact that in the original application of the situs statutes the Ohio taxing authorities sought to eliminate any due process objection by requiring a more substantial connection between the taxed intangible and the state taxing power than the single test of origination prescribed by Section 5328-2, General Code. This substantial connection was reflected in Rule 204 of the Tax Commissioner which necessitated control and management of the intangibles in the non-residential state and in the requirement of the Board of Tax Appeals that the intangibles not only arise out of business in such other state but that the intangibles be so used as to become an integral part of the business carried on in such state.

The Supreme Court deemed it inappropriate to decide whether the fact that the receivables in question arose from the shipment of a stock of goods maintained in Ohio was a sufficient nexus between the property and the taxing power to sustain the taxation thereof under the due process clause.[47] The Court found a more immediate constitutional problem in that it determined that the taxation of the accounts receivable of foreign corporations under the single test of origination prescribed by Section 5328-2, as interpreted by the Ohio Supreme Court, resulted in discrimination against such taxpayer in favor of domestic corporations and therefore denied them equal protection of the law.[48] In Paragraph 1 of its syllabus the Supreme Court stated:

> The state action which is reviewable under the Fourteenth Amendment is the composite result of both legislation and its judicial interpretation.

Thus, the Supreme Court concluded that for the purpose of judicial review the interpretation of the Ohio taxing statutes by the Ohio Supreme Court became a part of the situs statutes. The interpretation of the situs statutes in the *Ransom* case with respect to a domestic corporation was therefore to be tested constitutionally when the same theory was applied to the taxation of intangible property belonging to a foreign corporation. The Supreme Court referred to the

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[47] UNITED STATES CONST. AMEND. XIV § 1, provides:

"All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

[48] *Ibid.*

administrative policy of the Tax Commissioner which was formulated in conformity with the decision of the Ohio Supreme Court in the *Ransom* case. Under this administrative policy the situs statutes were applied so as to exempt from taxation in Ohio accounts receivable of Ohio residents, which arose:

> 1. From a sale of goods by an agent having an office in another state, even though such goods be shipped from Ohio, or
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> 2. From a sale of goods shipped from another state, even though such goods be sold by an agent having an office in Ohio.[49]

Conversely, the administrative policy subjected to taxation in Ohio the accounts receivable of non-residents of Ohio which arose:

> 1. From a sale of goods shipped from Ohio, even though such goods were sold by an agent having an office outside of Ohio, or
>
> 2. From a sale of goods by an agent having an office in Ohio, even though such goods were shipped from another state.

This administrative policy was compelled by the decision of the Ohio Supreme Court in the *Ransom* case which held that Section 5328-2, General Code, fixed the situs of accounts receivable in and out of Ohio.

As a preface to its remarks on the equal protection defect in the Ohio situs statutes as applied to the foreign corporations, the Supreme Court held that because Ohio had admitted these foreign corporations to carry on intrastate business within its borders, such corporations were entitled to equal protection of the law with respect to ad valorem taxation of their property.[50] The discriminatory effect of Ohio situs statutes as applied to the taxation of accounts receivable of a foreign corporation was pointed out by the Supreme Court in the following supposition:

> If on the taxing date one of these petitioners and an Ohio competitor each owns an account receivable of the same amount from the same out-of-state customer for the same kind of commodity, both shipped from a manufacturing plant in Ohio and both sold out of Ohio by an agent having an office out of the State appellant's account receivable

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[49] OHIO GEN. CODE § 5328-2.

[50] The Supreme Court stated:

"After a state has chosen to domesticate foreign corporations, the adopted corporations are entitled to equal protection with the state's own progeny, at least to the extent that their property is entitled to an equally favorable ad valorem tax basis."

> would be subject to Ohio's ad valorem tax and the one held by the competing domestic corporation would not.

Stress was placed on the fact that the Ohio situs statutes as judicially interpreted created a situation where under identical factual circumstances the receivables of foreign corporations would be taxable in Ohio whereas those of a domestic corporation would not. This inequality, it was said, did not result because of any difference "in Ohio's relation to the decisive transaction, but solely because of the different residence of the owner." The conclusion seems inescapable but that this result stems from the interpretation of the situs statutes in such a way that the provisions of Section 5328-2, General Code, were deemed controlling in fixing the business situs of accounts receivable. The requirement that the accounts receivable be "used in business in such other state" as prescribed in Section 5328-1, General Code, is virtually nullified because the Ohio Supreme Court held that the "used in business" test was met if the receivables were applied or were intended to be applied in the taxpayer's business whether in Ohio or elsewhere.[51]

It was further concluded by the Supreme Court that the reciprocal provisions of the situs statutes did not cure the lack of equal protection with respect to foreign corporations. With respect to the situs formula, the Court stated:

> The plan may be said to be logically consistent in that, while it draws all such intangibles of non-residents within the taxing power of Ohio, it by the same formula excludes those of residents.

The Court, however, did not feel that Ohio's proffered reciprocity restored to the foreign corporations the equality which the application of the situs statutes denied them. Emphasis was placed by the Court on the lack of any willingness by other states to adopt situs statutes similar to Ohio in order to tax those intangibles which Ohio exempts. The Court pointed out that the state of West Virginia taxed all the accounts receivable of the Wheeling Steel Corporation on the basis of the common law business situs doctrine.[52] In this connection it was said:

> Far from acceding to the situs doctrine which allocates these receivables to Ohio, The State of West Virginia stands

[51] In referring to the different interpretations of the situs statutes by the Board of Tax Appeals and the Ohio Supreme Court, this observation was made by the Supreme Court: "It was this requirement (the requirement of the Board that the intangibles be used so as to become an integral part of the local business) which the Supreme Court of the State eliminated in Ransom & Randolph Co. v. Evatt, 142 Ohio St. 398, 27 O.O. 348, 52 N.E. 2d. 738, when it held that any use of the intangibles in the general business was sufficient to make them taxable."

[52] *Supra*, note 17.

> on the very different situs doctrine approved by this Court in Wheeling Steel Corp. v. Fox . . . and under its authority has for the year in question taxed all of the receivables of the Wheeling Company, including those Ohio seeks to claim as having situs in Ohio.

It was concluded by the Supreme Court that the reciprocal provisions of the Ohio statutes did not protect non-residents against the discrimination which the Court found present in the situs statutes. The gist of the Supreme Court's decision is reflected in Paragraph 5 of the syllabus which reads as follows:

> A state ad valorem tax against certain intangible property such as notes and accounts receivable, owned by foreign corporations and owing from out-of-state debtors, which at the same time exempts identical property owned by residents and domestic corporations, is invalid as violating the equal protection clause of the Fourteenth Amendment; and equality is not restored by the fact that the exempted intangibles of residents are offered up to the taxing power of other states.

Reflections On The Ransom Case—A Quest For Equality

The decision of the United States Supreme Court holding that the Ohio situs statutes denied equal protection of the law to foreign corporations compels a re-examination of the Ohio situs statutes relative to accounts receivable as interpreted in the *Ransom* case. The press of candor necessitates the observation that any present reflections on the doctrine laid down in the *Ransom* decision benefit from the certitude of hindsight.

In the *Proctor and Gamble, Ransom and Randolph* and *Haverfield* [53] cases the Ohio Supreme Court interpreted the situs statutes with respect to the establishment of a business situs out of Ohio of accounts receivable of Ohio corporations. The question of constitutional limitations was not present, for Section 5328-1 subjects all of the intangibles of an Ohio resident to taxation unless certain of those intangibles have acquired a business situs outside Ohio. This basic portion of Section 5328-1, which taxes all the intangibles of an Ohio resident, is in accord with the constitutional authority of the state of domicile to tax the intangibles of its residents.[54] In the *Ransom* decision the Court did not concern itself with common law principles relative to the business situs of accounts receivable, for the Court found that the tests of business situs were supplied by Sections 5328-1 and 5328-2, General Code.

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[53] 142 Ohio St. 369, 52 N.E. 2d 517 (1943); 142 Ohio St. 398, 52 N.E. 2d 738 (1944); 143 Ohio St. 58, 54 N.E. 2d 149 (1944). In the *Haverfield* decision the Court followed the doctrine of the *Ransom* case.

[54] Curry v. McCanless, 307 U.S. 357 (1939).

A perusal of the situs statutes reveals that such statutes lend themselves to the interpretation taken by the Court in the *Ransom* case when the accounts receivable are owned by Ohio residents. Section 5328-1 provides that the intangibles mentioned in Section 5328-2 shall have a business situs out of Ohio if such intangibles are used in and arise out of business transacted in another state. For the definition of the "used in business" portion of the business situs test the Court turned to Section 5325-1, General Code, which defines the term "used in business." The Court further concluded that Section 5328-2 fixes the business situs of accounts receivable and that if the accounts receivable of a domestic corporation meet the test of that section and are used in business as mentioned in Section 5325-1, then such receivables have a business situs outside of Ohio. The conclusion of the Court that Section 5328-2 fixes the business situs of accounts receivable finds support in the last paragraph of such Section, which provides that:

> The provisions of this section shall be reciprocally applied, to the end that all property of the kinds and classes mentioned in this section having a business situs in this state shall be taxed herein and no property of such kinds and classes belonging to a person residing in this state and having a business situs outside of this state shall be taxed.

This portion of Section 5328-2 states that the provisions of this section shall be reciprocally applied to establish a business situs in and out of Ohio.

Despite the fact that the situs statutes are subject to the interpretation placed upon them by the Court with respect to domestic corporations, there is need for another interpretation of these statutes because the application of the *Ransom* doctrine to the accounts receivable of a foreign corporation has resulted in an unconstitutional application of the statutes.[55] The effect of the United States Supreme Court's decision is of importance to both domestic and foreign corporations because Section 5328-2 further provides that:

> If any provision of this section shall be held invalid as applied to property of a non-resident person, such decision shall be deemed also to affect such provision as applied to property of a resident, but shall not affect any other provision hereof.

The question is: May the Ohio situs statutes be interpreted in such a manner so that the establishment of a business situs outside of Ohio for intangibles of domestic corporations may be reciprocally

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[55] Wheeling Steel Corp. v. Glander; National Distillers Products Corp. v. Glander, 337 U.S. 562 (1949).

applied to foreign corporations without a constitutional impediment? It is submitted that such an interpretation can be made, and in order to do so attention must be focused on the "used in business" portion of the test of business situs set forth in Section 5328-1, General Code. It will be recalled that the Court in the *Ransom* case concluded that accounts receivable were "used in business" if such receivables meet the definition of Section 5325-1 in that they or the avails thereof are being applied or are intended to be applied in the conduct of the business whether in this state or elsewhere. Under this interpretation of "used in business" it would seem that any use of the intangibles in the general business is sufficient.[56] It should be emphasized that Section 5328-1 initially subjects all the intangibles of Ohio residents to taxation and then provides that certain intangibles mentioned in Section 5328-2 used in and arising out of business transacted out of Ohio shall not be subject to taxation. With respect to non-residents of Ohio it was declared that the intangibles mentioned in Section 5328-2, used in and arising out of business transacted in Ohio, shall be subject to taxation. Thus, Section 5328-1 imposes a dual test for the establishment of a business situs of accounts receivable in or out of Ohio. The requirement is not that the accounts receivable be used in business generally, but that they be used in Ohio or out of Ohio. For example, with respect to foreign corporations, Section 5328-1 taxes the intangibles of such corporations "used in and arising out of business transacted in this state." The use of the conjunction "and" between the dual test "used in" and "arising out of" suggests that the receivables must be used in business in Ohio and arise out of business in Ohio.

Under the view taken by the Ohio Supreme Court, accounts receivable are used in business if used in the general business of the taxpayer, whether in Ohio or elsewhere. The use of accounts receivable in the general business of the company does not fulfill the requirement of Section 5328-1 that such receivables of non-residents be used in this state and that receivables of residents be used out of this state. The function of Section 5328-1 is to establish tests for determining business situs of intangible property in and out of Ohio. The fixation of a situs of accounts receivable in or out of Ohio requires the use of the intangible property within a specific taxing sovereign and not a general use of such intangible in the taxing sovereign or in other states.

Is the term "used in business" which is used in Section 5328-1 as part of the test of business situs defined by Section 5325-1, General Code? It is submitted that it can reasonably be concluded that the definition of "used in business" in Section 5325-1 has no connection

[56] *Supra*, note 51.

with the "used in business" term of Section 5328-1 which relates to the establishment of a business situs of accounts receivable. Section 5325-1 has two primary functions:

> (1) The section defines the term "used in business" with respect to tangible personal property so as to determine what tangible personal property is subject to taxation.[57] Under Section 5328, General Code, "all personal property located and used in business in this state" is subject to taxation. In other words, the "used in business" definition of Section 5325-1 first of all draws the line of taxability between tangible property which is used in business and that which is not. For example, the furniture which is located in a private home does not meet the qualifying test of "used in business" as prescribed in Section 5328 and as defined in Section 5325-1, and hence is not subject to taxation. But the tangible personal property utilized in the operation of a grocery store meets the test of "used in business" under Sections 5325-1 and 5328, and is subject to the personal property tax.
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> (2) With respect to intangible property, Section 5325-1 serves two purposes. The section defines the terms "used in business" or "used" with respect to intangible property by providing that intangible property "shall be considered to be 'used' when they or the avails thereof are being applied, or are intended to be applied in the conduct of the business, whether in this state or elsewhere." Accounts receivable which meet this test of "used in business" are taxed as credits as prescribed in Section 5327, General Code.[58] Under such section the excess of current accounts receivable and prepaid items used in business over and above current accounts payable is considered to be taxable credits.

A further purpose which the definitive provisions of Section 5325-1 serve with respect to intangible property is that such section

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[57] OHIO GEN. CODE §§ 5325, 5325-1, 5328, 5367, 5368, 5370 to 5388 and related sections. The basic rule of § 5328 is that tangible personalty as defined in § 5325 must be "used in business" to be taxable. However, under § 5328 domestic animals, ships, vessels and boats, and aircraft are taxable whether "used in business" or not.

[58] OHIO GEN. CODE § 5327 provides in part:

"The term 'credits' as so used, means the excess of the sum of all current accounts receivable and prepaid items used in business when added together estimating every such account and item at its true value in money, over and above the sum of current accounts payable of the business, other than taxes and assessments. 'Current accounts' includes items receivable or payable on demand or within one year from the date of inception, however evidenced."

provides which intangibles are subject to allocation in or out of Ohio under the business situs theory established by the situs statutes. A qualifying provision of Section 5328-2 is that the property mentioned therein be "used in business." The initial provision of the Section reads as follows:

> Property of the kinds and classes herein mentioned, *when used in business,* shall be considered to arise out of business transacted in a state other than that in which the owner thereof resides in the cases and under the circumstances following: . . . . (Emphasis supplied.)

Hence, under this qualification only the intangibles which are used in business may acquire a business situs in or out of Ohio. If the intangible property of an Ohio resident is not used in business as required by Section 5328-2, and as defined by Section 5325-1, all of such person's intangibles are taxable in Ohio.[59] For example, all of the money of an Ohio resident is subject to taxation in Ohio if such money cannot be said to be "used in business," whereas money which meets the test of "used in business" may acquire a business situs outside of Ohio under the provisions of Sections 5328-1 and 5328-2, General Code. Furthermore, only those intangibles of a non-resident which are "used in business" as required by Section 5328-2 and as such term is defined in Section 5325-1, may acquire a business situs in Ohio under the situs statutes so as to be subject to taxation in this state.

The argument that the "used in business" requirement of Section 5328-1 with respect to fixing a situs of intangible property in or out of Ohio is not defined by the general definitive provisions of Section 5325-1 is supported by reference to the last sentence in Section 5325-1, General Code. Such section defines the term "used in business" and "business" is defined as:

> 'Business' includes all enterprises of whatsoever character conducted for gain, profit or income and extends to personal service occupations.

Thus, it is apparent that the General Assembly was setting up a standard by which the administrative officer could determine which tangible and intangible property was "used in business" and which such property was not so used. The definitive provisions of Section 5325-1 are general in nature and provide tests of when property

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[59] Intangible property of Ohio residents is taxable irrespective of whether such property is "used in business." § 5328-1 initially subjects all of the enumerated intangibles of residents to taxation. Under §§ 5328-1 and 5328-2, however, intangibles of residents may gain a tax situs out of Ohio and intangibles of non-residents may acquire a tax situs in Ohio only if such intangibles are "used in business" as required by § 5328-2 and as such term is defined in § 5325-1.

may be said to be used in business as part of a commercial enterprise. As before adverted to, whether or not tangible personal property is used in business determines the taxability of such property under Section 5328, General Code. With respect to intangible property, whether such property may be said to be used in business determines the manner in which accounts receivable are taxed and generally whether or not intangible property may be allocated in or out of Ohio pursuant to the situs statutes.

If the view be taken that Section 5325-1 does not define the term "used in business" when such term is used in connection with the establishment of a business situs for intangible property, the sequent conclusion would be that Section 5328-2 is operative to establish the "arising out of business in such other state" but the "used in business" test of Section 5328-1 would be established by reference to common law principles of business situs. The Ohio Board of Tax Appeals interpreted the "used in business" requirement in the *Ransom* case by requiring that the accounts receivable be used so as to become an integral part of the business conducted in such other state. Rule 204 of the Tax Commissioner, which was considered by the Ohio Supreme Court in the *Ransom* case, also relied upon the common law requirement that the intangible property be controlled and used in the non-domiciliary state. The difference between the view of "used in business" with reference to establishing the business situs of accounts receivable as interpreted by the Court in the *Ransom* case and as required under common law principles is readily discernible. The Ohio Supreme Court said that any use of the accounts receivable in the business activities of the taxpayer, either in this state or elsewhere, was sufficient and the Court based its conclusion upon the definitive provision of Section 5325-1, General Code. The common law view requires generally that the intangibles be used and controlled in a localized business in the taxing sovereign. In the previously mentioned *Kelly-Springfield Tire Company*[60] case the Court referred to an opinion of the Ohio Attorney General[61] in which the following comment was made on the common law business situs theory:

> Credits of a non-resident corporation may be taxed in Ohio, only when they are 'localized' by being committed to the charge and management of an agent or other representative who is more than a mere custodian or collector and who has power to deal in a managerial capacity with the fund represented by the credit.

The common law view of business situs is illustrated in the case of

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[60] *Supra*, note 23.

[61] 1912 OPS. ATT'Y GEN. (Ohio) Vol. I, No. 453.

Wheeling Steel Corp. v. Fox.[62] The Wheeling Steel Corporation carried on most of its business activities in the state of West Virginia. It had established there what the United States Supreme Court referred to as a "commercial domicile." Said corporation maintained its general business offices in West Virginia and there it kept its books and accounting records. The business activities of the corporation in West Virginia were commented on by the Supreme Court as follows: "The Corporation has made that the actual seat of its corporate government."

With respect to the accounts receivable which arose by sales of the Wheeling Steel Corporation from manufacturing plants outside of West Virginia, the Supreme Court stated:

> The accounts are not necessarily localized in whole or in part where the goods are made but are attributable as choses in action to the place where they arise in the course of the business of making contracts of sale.

More recently, in the case of *Newark Fire Insurance Co. v. State Board of Tax Appeals,*[63] the United States Supreme Court made some explanatory statements relative to the business situs of accounts receivable. The Court said:

> * * * There are occasions, however, when the use of intangible personalty in other states becomes so inextricably a part of the business there conducted that it becomes subject to taxation by that state.

This further comment was made by the Supreme Court:

> Where consideration has been given to the existence of a business situs of intangibles for taxation by a state other than the state of domicile, there has been definite evidence that the intangibles were integral parts of the business conducted. In so far as the conclusion as to the existence of a business situs for the purpose of taxation, distinct from the domiciliary situs, is the basis for a claim of a Federal right, the duty of inquiring into the evidence which establishes such business situs rests upon this Court.

Because of factual variants no all-inclusive rule may be stated which establishes the business situs for accounts receivable in a non-domiciliary state. However, the Supreme Court has indicated that such accounts receivable must be used in the non-domiciliary state so as to become an integral part of the local business.

If the common law view of the "used in business" requirement of Section 5328-1 be adopted, it would seem that equality between Ohio residents and non-residents of this state could be established

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[62] 298 U.S. 193 (1936).

[63] 307 U.S. 313 (1939).

in the taxation of accounts receivable. Under this suggested approach a common standard for the establishment of a business situs in and out of Ohio would be required. In addition to the requirement that the accounts receivable arise out of business in such other state under the provisions of Section 5328-2, it would further be necessary for the establishment of a business situs that such receivables be used in business in such other state so as to become an integral part of the local business. The constitutional defect which was found in the situs statutes of Ohio when applied to a foreign corporation stems from the fact that the "used in business" requirement of Section 5328-1, was virtually nullified by the interpretation thereof in the *Ransom* decision which held that accounts receivable were "used in business" when such property was applied or was intended to be applied in the conduct of the business, whether in this state or elsewhere. Thus, in practical effect, the only test for the establishment of a business situs in or out of Ohio was resolved by the application of the test of origination under Section 5328-2, General Code. It is submitted, however, that Sections 5328-1 and 5328-2, together establish a business situs for intangibles. Section 5328-2 is not self-executing. The declaration of legislative policy in establishing a business situs for intangibles in and out of Ohio is contained in Section 5328-1, General Code. Section 5328-1 is the levying section which initially taxes all the intangibles of Ohio residents but then further prescribes that certain of such intangibles owned by residents may gain a business situs outside Ohio; and such section also provides for the ascribing of a business situs in Ohio to those intangibles of non-residents which are mentioned in Section 5328-2, General Code.

Under the *Ransom* decision accounts receivable of a resident could acquire a business situs out of Ohio if such receivables arose out of business out of Ohio in one of the three ways set forth in such Section 5328-2, and if the receivables were used in the general business of the taxpayer in order to meet the definitive test of Section 5325-1, General Code. As applied to a foreign corporation, this theory was found to be discriminatory because business situs became solely dependent upon the arising out of business provisions of Section 5328-2, General Code. As pointed out by the United States Supreme Court, the establishment of a business situs for accounts receivable under Section 5328-2 can result in the exemption of such receivables of a domestic corporation, while under an identical factual situation the receivables of a foreign corporation would be taxable in Ohio. This discrimination could be obviated if in addition to the provision of Section 5328-2 that the accounts receivable arise out of business in or out of Ohio, there be imposed the requirement that such accounts receivable must be used in business in or out of Ohio within the

purview of the common law principles of business situs. The lack of equal protection with respect to foreign corporations which the Supreme Court found in the Ohio situs statutes as judicially interpreted, makes it patent that there is need for a common standard with respect to the establishment of a business situs of accounts receivable in or out of Ohio.

In the *Ransom* case the Ohio Supreme Court made the observation that the Ohio situs statutes were enacted to avoid the possibility of intangibles being taxed in more than one state. In this connection the Court said:

> It is clear that it was the intention of the General Assembly that all property having a business situs in Ohio should be taxed in Ohio and that no property having a business situs outside of Ohio should be so taxed.
>
> It was to avoid the application of the principle recognized in *Fidelity & Columbia Trust Co., Exr. v. City of Louisville,* 245 U. S. 54 . . . that liability to taxation in one state does not necessarily exclude liability in another, that the legislation here under consideration was passed.

Whether or not the rationale of the *Ransom* case, when carried to its ultimate, would avoid the possible taxation of the same intangible in more than one state provokes an interesting question. In the *Fidelity & Columbia Trust Co.* case,[64] Justice Holmes, in writing for the Court, stated that: "But liability to taxation in one state does not necessarily exclude liability in another." The Supreme Court concluded that the deposits of an individual were taxable in the state of his domicile even though the same deposits could have been taxed by the non-domiciliary state where such deposits arose out of business therein.

More recently, in *Curry v. McCanless,*[65] the Supreme Court has indicated that an intangible may be taxed by more than one state. In paragraph fifteen of the syllabus it was stated: "The Fourteenth Amendment does not require the fixing of a single exclusive place for the taxation of intangibles." The *Curry* case upheld the imposition by the states of Alabama and Tennessee of death taxes in a situation where a resident of Tennessee created a trust of intangibles by vesting legal title to such intangibles in the Alabama trustee. The donor provided that by her power to dispose of property by will, such power being conferred by the state of domicile, the trust could be terminated and the property would pass under the will. Although the *Curry* case deals with the imposition of death taxes, the case is a review of the principles

[64] *Supra,* note 36.

[65] 307 U.S. 357 (1939).

announced by the Supreme Court in dealing with the situs of intangible property. In the course of its opinion, the Court referred to the fact that a taxpayer who is domiciled in one state but who carries on a business in another state is subject to taxation in the state where the intangibles are used in business. In support of this statement the Court cited, among other cases, *Wheeling Steel Corporation v. Fox.*[66] The Court made this significant statement:

> But taxation of a corporation by a state where it does business, measured by the value of the intangibles used in its business there, does not preclude the state of incorporation from imposing a tax measured by all of its intangibles.

It is interesting to note that Mr. Justice Reed, while concurring in the majority opinion, reserved his conclusions as to the above quoted portion of the majority opinion.

In *Tax Commission v. Aldrich*[67] the Supreme Court had before it the question of whether the state of Utah was precluded by the Fourteenth Amendment from imposing a tax upon a transfer by death of shares of stock in a Utah corporation, such stock being part of the estate of the decedent who at the time of his death was domiciled in New York, and there held the stock certificates. The Court upheld Utah's taxation of such shares and in so doing they overruled *First National Bank v. Maine*[68] which had read into the Fourteenth Amendment an immunity from taxation of intangibles by more than one state. In the *Aldrich* case the Court discusses the basic rules relating to the jurisdiction of states to tax intangible property. It is pointed out that intangibles may be subject to taxation by a state other than the state of domicile if the non-domiciliary state has sufficient connection with the intangible to give such state the jurisdiction to tax. The tenor of the Court's opinion is reflected in the following statement:

> In line with our recent decisions[69] * * * we repeat that there is no constitutional rule of immunity from taxation of intangibles by more than one State. In case of shares of stock 'jurisdiction to tax' is not restricted to the domiciliary state. Another State which extended benefits or protection or which can demonstrate 'the practical fact of its power' or sovereignty as respect the shares * * * may likewise constitutionally make its exaction.

Reference has been made to the various expressions of the United States Supreme Court relative to the doctrine that the

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[66] 298 U.S. 193 (1936).

[67] 316 U.S. 174 (1942).

[68] 284 U. S. 312 (1932).

[69] Curry v. McCanless, 307 U.S. 357 (1939); Graves v. Elliott, 307 U.S. 383 (1939); Graves v. Schmidlapp, 315 U.S. 657 (1942).

Fourteenth Amendment does not fix a single situs for the taxation of intangible property, in order to discuss the implications of the statement by the Ohio Supreme Court in the *Ransom* case that the Ohio situs statutes were intended to avoid the application of such doctrine. There is no reason to doubt that the Ohio General Assembly was cognizant of the possible taxation of intangible property by various states, for the situs statutes clearly reflect legislative intention to avoid multiple taxation of intangible property. The situs statutes recognize that accounts receivable of Ohio residents may acquire a business situs outside of Ohio and could be subject to taxation out of Ohio. Hence, to avoid taxation of such accounts receivable by the state of business situs and by Ohio under its taxing powers as the state of domicile, the General Assembly provided that those receivables acquiring a business situs outside of Ohio should not be taxed in this state.

Do the situs statutes as interpreted in the *Ransom* decision avoid the application of the principle referred to by the Ohio Supreme Court that taxation of intangibles in one state does not necessarily exclude such intangibles from taxation in another state? If the rationale of the *Ransom* case is carried to its ultimate, it is doubtful if the Ohio situs statutes would aid in preventing multiple taxation of intangibles. As the situs statutes were interpreted in the *Ransom* case, accounts receivable could acquire a business situs in or out of Ohio if receivables were used in the general business of the taxpayer and arose out of business transacted in or out of Ohio under the test of origination prescribed by Section 5328-2, General Code. Hence, accounts receivable of foreign corporations[70] were determined to have a business situs in Ohio because such receivables were used in the general business of the foreign corporations and arose from the shipment of a stock of goods located in Ohio. Under this interpretation accounts receivable would acquire a business situs in or out of Ohio if they were used in business within the purview of Section 5325-1, and if the receivables arose out of business in a state out of Ohio or in Ohio:

(1) from the sale of property sold by an agent having his office in such state, or

(2) from a stock of goods maintained therein, or

(3) from services performed by an officer, agent or employee connected with, sent from, or reporting to any officer or at any office located in such state.[71]

If for example, an Ohio corporation maintained stocks of goods in

[70] Wheeling Steel Corp. v. Glander; National Distillers Products Corp. v. Glander, 337 U.S. 562 (1949).

[71] OHIO GEN. CODE § 5328-2.

various states outside Ohio and these states were to adopt statutes similar to Ohio, then, as the Ohio law has been interpreted, each state from which receivables arose from a shipment of a stock of goods in such state could tax such receivables under the theory that the receivables had acquired a business situs in such state. The same situation would prevail if an Ohio corporation sold goods by agents having an office in various states outside of Ohio. Conversely, if other states were to adopt the situs statutes which Ohio has and were to interpret such statutes in conformity with the *Ransom* decision, then the receivables of foreign corporations that arose from sales of agents, from stocks of goods, or by the services of an officer or an agent in such other states, could be subject to multiple taxation. It will be recalled that in the *Wheeling Steel Corp. and National Distillers* case[72] in which the United States Supreme Court found the application of the Ohio situs statutes to foreign corporations to be violative of equal protection of law, the facts showed that both foreign corporations had manufacturing plants and stocks of goods in states other than Ohio. Therefore, those states other than Ohio could impose taxes on such receivables if the Ohio interpretation of business situs were adopted.

These observations relative to possible multiple taxation of accounts receivable which could arise under the interpretation of business situs announced in the *Ransom* case are made without reference to the fact that a due process question would undoubtedly be created by such multiple taxation.[73] Rather, the expressions as to the practical effect of the Ohio situs statutes as interpreted are designed to show that the adoption of the proposed interpretation of the situs statutes in conformity with the common law principles of business situs would, in addition to curing the consitutional objection to such situs statutes, also tend to prevent multiple taxation of intangibles.

If the Ohio situs statutes and other state intangible tax statutes were interpreted under the common law principles of business situs, the requirement that the intangibles be integrated in the local business[74] would, it is believed, impose definite limitations on multiple taxation of intangibles. Thus, if an Ohio corporation made another state the seat of its corporate government and its accounts receivable were integrated in such local business, then under the situs statutes Ohio would relinquish its right to tax as the state of domicile and would recognize the right of the business situs state to tax. It is submitted that the common law requirement that

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[72] 337 U. S. 562 (1949).

[73] Wisconsin v. J. C. Penny Co., 311 U.S. 435 (1940).

[74] Wheeling Steel Corp. v. Fox, 298 U. S. 193 (1936); Newark Fire Insurance Co. v. State Board of Tax Appeals, 307 U. S. 313 (1939).

there be a substantial connection between the intangibles and the taxing sovereign for accounts receivable to acquire a business situs outside the domiciliary state would aid in preventing the taxation of the same accounts receivable by various states because that connection would not be duplicated in the various states. In other words, it is unlikely that the same accounts receivable would be integrated in the business of more than one state.

CONCLUSION

The power of taxation must be confined within constitutional bounds. Ohio encountered this constitutional interdiction when the Ohio situs statutes were applied so as to tax the accounts receivable of foreign corporations which arose from shipments from stocks of goods located in Ohio.

Section 5328-1, General Code, initially subjects all the intangibles of Ohio residents to taxation. This section further provides for the allocation of intangibles in and out of Ohio. Accounts receivable of residents which are used in and arise out of business transacted outside of Ohio are not subject to taxation, whereas receivables of non-residents which are used in and arise out of business transacted in Ohio are subject to taxation. The interpretation of the situs statutes was determined in the *Ransom* case wherein the Court held that the only conditions for receivables of a domestic corporation to gain a business situs outside of Ohio are (1) that the receivables be "used in business" whether in this state or elsewhere within the purview of Section 5325-1, General Code, and (2) that the receivables "arise out of business transacted in such other state" under the test of origination prescribed by Section 5328-2, General Code. The Ohio Supreme Court ruled that Section 5328-2 fixed the business situs of acounts receivable.

The rationale of the *Ransom* case which announced the requisites for intangibles of a domestic corporation to gain a business situs outside Ohio was applied conversely to foreign corporations because of the reciprocal situs provisions of Section 5328-2, General Code. The United States Supreme Court held that the application of the theory of the *Ransom* case to the receivables of foreign corporations denied the equal protection of law to these foreign corporations, for under the test of origination prescribed by Section 5328-2, General Code, identical factual circumstances could result in the exemption of accounts receivable of a domestic corporation and the taxation of receivables belonging to foreign corporations.

The unconstitutional application of the Ohio situs statutes to accounts receivable of foreign corporations compels a different interpretation of the situs statutes from that announced in the

Ransom case. A common standard for ascribing a business situs for accounts receivable in and out of Ohio could be achieved if a dual test were imposed under the situs statutes. The dual test would require that the receivables be used in business and arise out of business in the non-residential state. The "used in business" portion of the business situs test imposed in Section 5328-1, would be interpreted in accordance with common law principles of business situs. The second facet of the business situs test imposed by Section 5328-1 would be resolved by the test of origination for accounts receivable prescribed by Section 5328-2, General Code. It is submitted that this dual test would establish equality between residents and non-residents with respect to the establishment of a business situs for accounts receivable in and out of Ohio, and if such dual test were uniformly applied by the various states, it would be a potent force in preventing multiple taxation of intangibles.